

TELRIC:
The Only Proven Methodology For
Reliably Pricing Unbundled Network
Elements

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OVERVIEW

- TELRIC remains best methodology for pricing UNEs.
- TELRIC achieves pricing goals of 1996 Act.
 - Reliably identifies costs.
 - Permits recovery of forward-looking costs of UNEs.
 - Sends efficient entry and investment signals.
- Use of ILECs' versions of "actual costs" would be inefficient and problematic.

TELRIC Remains Best Methodology for Pricing UNEs

- TELRIC is most efficient method for valuing networks:
 - Not disputed that most accurate way to value existing equipment is by measuring cost of new equipment that provides same functionality.
 - Also, the value of an existing network can be estimated by constructing a model of a newly built network.
- Efficient pricing provides numerous benefits, including:
 - Sending right signals to investors.
 - Sending right signals to consumers.
 - Helping deter price squeezes.

TELRIC Remains Best Methodology for Pricing UNEs

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- Availability of UNEs priced at TELRIC rates stimulates CLEC investment by enabling CLECs to overcome barriers to entry and enter market.
- States commissions, which have been applying TELRIC, contend that radical reform is not needed.
- Supreme Court upheld TELRIC less than two years ago.
- ILECs have been using forward looking cost models for decades.

TELRIC Achieves Pricing Goals of 1996 Act

Reliably Identifies Costs

- TELRIC is best method for properly attributing costs to individual network elements.
 - Accurate cost attribution more important than ever given that fewer and fewer network elements are subject to unbundling.
- TELRIC is most transparent and verifiable method of establishing costs.
 - Bottom up method operates with known formula.
 - Inputs primarily derived from publicly available data.
 - Assumptions are express and open to challenge.
 - Allows for simulations to be run.
- Models incorporate real-world data where reliable and verifiable data exists.

TELRIC Achieves Pricing Goals of 1996 Act

Permits Recovery of Forward Looking Costs of UNEs

- Most accurate way to value existing network is by measuring cost of new network that provides same functionality.
- Cost models used by state commissions have increased in sophistication and granularity.
 - Models incorporate real-world factors that affect costs.
- ILECs have appropriate influence on rate determinations:
 - Proceedings permit ILECs to provide data and analyze and assess models and inputs used to set UNE rates.

TELRIC Achieves Pricing Goals of 1996 Act

Permits Recovery of Forward Looking Costs of UNEs

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- Goal of UNE costing is to determine cost of providing regulated network function. TELRIC enables entire cost of facilities to be determined and recovered on a comprehensive and internally consistent basis.
- TELRIC has not resulted in unduly low UNE rates.
 - ILECs leasing UNEs continue to post strong balance sheets.

TELRIC Achieves Pricing Goals of 1996 Act

Permits Recovery of Forward Looking Costs of UNEs

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- TELRIC should not be changed simply because it does not enable recovery of book value/embedded costs.
 - ILECs greatly overstate gap between book and TELRIC costs.
 - Book cost includes costs of elements not made available as UNEs.
 - Book cost includes retail service expenditures that are not provided to wholesale customers.
 - Book cost includes items efficient providers would not have built.
 - There are no book cost measures that provide necessary disaggregate detail for rate deaveraging.

TELRIC Achieves Pricing Goals of 1996 Act

Sends Efficient Entry and Investment Signals

- Rates are set high enough to encourage CLECs to build their own facilities in appropriate situations.
 - CLECs invested approximately \$71 billion from 1996 through 2002.
- Helps prevent inefficient and anticompetitive “price squeezes.”
- TELRIC encourages economically efficient amount of ILEC facilities investment because it is designed to provide ILECs with appropriate return on investment.
 - In any event, elements made available to CLECs are provided primarily by sunk investments and are in abundant supply.

Use of ILECs' Versions of "Actual Costs" Would be Inefficient and Problematic

- Use of "actual costs" would raise significant problems and not improve accuracy or consistency.
 - There are no "actual costs" on ILECs' books; a method relying on "actual costs" would itself involve cost modeling.
 - Difficult to draw assumptions about cost of individual UNEs from existing network because it was built to provide many different services, some of which are unrelated to cost of UNEs.
 - Use of existing network data would result in informational asymmetries because regulators and competitors would be limited to data produced by ILECs.

Use of ILECs' Versions of "Actual Costs"

Would be Inefficient and Problematic

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- Models that "reconstruct network over time," rather than current model of newly deployed network would be more complicated and cumbersome.
 - Would require modeling of different mixes of technology subject to different depreciation schedules.
 - Would require state commissions to resolve difficult valuation questions about value of older technology.
 - Would require greater reliance on data derived from ILECs' embedded networks, thus introducing embedded costs and giving ILECs an informational advantage.

Use of ILECs' Versions of “Actual Costs” Would be Inefficient and Problematic

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- Use of ILEC engineering assumptions about upcoming network changes in short term (three to five years) would be unduly complex and provide meaningless results.
 - Short-term expenditures do not reflect scale and scope economies of networks.
 - Short-term expenditures do not reflect ideal mix of network equipment, mix of equipment currently in network, or mix of equipment that will ever be in network.
 - Short-term data must be manipulated (*e.g.*, grossed up) to be useful, which detracts from its purported “real world” benefits.

Conclusion

- There is no choice but to rely on some type of model to estimate UNE costs.
- There is no measure of forward-looking “actual cost” that the ILECs can make available.
- The ILECs have been using forward-looking cost models for decades.
- By now, TELRIC models are well-tested and understood by the state commissions.